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Utah Supreme Court

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IN THE SUPREME COURT OF THE STATE OF UTAH

OWYHEE, INC., a corporation,
Plaintiff, garnishee plaintiff and appellant,

vs.

ROBBINS MARCO POLO, aka and dba ROBBINS MARK-O-POLO, a corporation, and ROBBINS TRAVEL INTERNATIONAL, INC., a corporation,
Defendants and judgment debtors,

vs.

DWIGHT G. LUMAN,
Garnishee defendant and respondent.

Case No. 10162

BRIEF OF APPELLANT

Appeal of Owyhee, Inc., from the Judgment of the District Court of Salt Lake County, State of Utah
Hon. Stewart M. Hanson, Presiding

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Defendants and judgment debtors,

vs.

DWIGHT G. LUMAN,
Garnishee defendant and respondent.

Case No. 10162

BRIEF OF APPELLANT

STATEMENT OF FACTS

This is a garnishee action by plaintiff, garnishee plaintiff and appellant (hereinafter called plaintiff) against garnishee defendant and respondent (hereinafter called defendant) based upon an alleged debt from defendant to judgment debtor Robbins Travel International, Inc. (hereinafter called Robbins, Inc.) arising out of assertedly illegal payment by Robbins, Inc. to defendant pursuant to a corporate note given defendant allegedly in the purchase of stock in Robbins, Inc. owned by defendant. The Trial Court, sitting without a jury, entered a decree dismissing the action (R. 18). On appeal, plaintiff prays that this Court reverse such decree and remand this case to the Trial Court with the direction to enter judgment against defendant and in favor of plaintiff in the sum of the judgment debt owing by Robbins, Inc. to plaintiff (R. 1), but not to exceed $1,900.00 (R. 5-6; Tr. 3).

The Trial Court likely did not "find the facts specially and state separately its conclusions of law thereon," as required by URCP 52(a). Rather, it characterized its memorandum decision (R. 16-17) as constituting such findings and conclusions (R. 18). In that the transcript is relatively brief and, moreover, because the pertinent objective facts are without dispute, the methodology adopted does not impede consideration of the salient issues. Such facts follow.

In February or March, 1960, defendant entered into a transaction with Robbins, Inc. through its president, Allen B. Robbins (Tr. 3-4, 16). The arrangement agreed upon was that defendant "would put money into Robbins Travel and would come in as an owner and as an officer" (Tr. 17). His ownership was to be of a given percent of the corporation — Mr. Robbins testified 40% and defendant recalled 48% (Tr. 5, 19), in exchange for $4,000.00 paid in (Tr. 20). It was also agreed that defendant would become a director (Tr. 20). At or about the time defendant came into the corporation and became an officer, vice-president, he did in fact pay in the $4,000.00 which was placed in a corporate account (Tr. 5, 7, 19-20). Mr. Robbins testified that defendant became a director, but defendant said that he never participated "in any kind of director activities" (Tr. 5, 20). A stock certificate was never delivered defendant for whatever number of shares the agreed percentage represented (Tr. 12-14, 17-18).

By April, 1960, the relationship between defendant and Robbins, Inc.'s president — Mr. Robbins — had become inamicable. According to defendant:

> "I wanted out of the corporation. I wanted my money out, and I wanted to terminate my employment there. This was agreeable with Mr. Robbins. As he has mentioned he was dissatisfied with my efforts and by mutual consent we agreed that I would leave." (Tr. 18).

Mr. Robbins' testimony was substantially identical (Tr. 10, 13, 15).

It was agreed that defendant would withdraw from Robbins, Inc. (Tr. 10, 13, 15, 18). On April 11, 1960, Mr. Robbins delivered to defendant a promissory note for the money he had put into the corporation, executed both by the corporation and personally (R. 11; Tr. 8-10, 13).

Payments of at least $1,900.00 were made prior to May 11, 1961, to defendant by Robbins, Inc. (Tr. 11-12, 18-19; Ex. D-1). The corporation was insolvent at the times of such payments, i.e. its liabilities exceeded its assets (Tr. 12).

Plaintiff's judgment against Robbins, Inc. (R. 1) was based upon an indebtedness incurred subsequent to such payments (Tr. 14).

ARGUMENT

POINT I

THE TRANSACTIONS HERE INVOLVED CONSTITUTED: (A) A SALE OF STOCK BY ROBBINS, INC. TO DEFENDANT; AND, LATER AND SEPARATELY, (B) A PURCHASE OF SUCH STOCK FROM DEFENDANT BY ROBBINS, INC.

Plaintiff characterizes as stock transactions both the agreement of February or March, 1960, by which defendant "put money into Robbins Travel and would come in as an owner" (Tr. 17) and the later agreement of April, 1960 satisfying defendant's desire to be "out of the corporation. I wanted my money out, and I wanted to terminate my employment there" (Tr. 18). Defendant disputes this denomination (R. 9). The Trial Court expressly refused to rule upon the character of the two transactions, stating: "This Court is not going to determine that this was a stock transaction or a loan transaction . . ." (R. 17).

A.

The initial agreement of February or March, 1960, *and payment by defendant thereunder, constituted defendant a stockholder in Robbins, Inc.*

There is no question that an integral part of the initial agreement between Robbins, Inc. and defendant was that the latter would become a part owner of the corporation. This was the testimony of Mr. Robbins, who handled the transaction for Robbins, Inc. (Tr. 5). More important, the defendant himself so stated (Tr. 17, 19). Although the two participants differed as to the percentage of ownership to be held by defendant, they concurred that defendant was to acquire such a percentage (Tr. 5, 19). It is further undisputed that — pursuant to such agreement and well in advance of the later agreement of April, 1960 — defendant did pay the $4,000.00 specified by the agreement into the corporation, and that it was placed in the corporation account (Tr. 5, 7, 19-20).

Based upon this recitation, it is patent that the agreement was not for defendant to make a $4,000.00 "loan" to the corporation, and that the $4,000.00 in fact paid in pursuant to such agreement did not constitute a "loan." Quite the contrary. According to defendant's own testimony (Tr. 17, 19), he became a part owner, not a creditor, of Robbins, Inc. through his payment.[1]

[1] On cross-examination, Mr. Robbins denied that the $4,0000.00 was a loan (Tr. 14). Neither on direct nor on cross did defendant so describe it. As noted, he in fact affirmatively indicated his ownership capacity (Tr. 17, 19).

It is elementary that acquisition of stock is the means by which one gains part "ownership" of a corporation 16-2-5(7) UCA, 1953 [2]; 13 *Am. Jur., Corporations* § 172. In consequence, the agreement was clearly for defendant to obtain a stock right, and defendant's testimony corroborates Mr. Robbins' more explicit recitation (Tr. 5) to that effect.

It is, of course, undisputed that defendant did not receive a stock certificate from Robbins, Inc. evidencing his stock interest (Tr. 12-14, 17-18). But "it is well settled that a certificate of stock in a corporation is not the stock itself," 11 *Fletcher, Cyc. Corps.* § 5092 at p .75; *Robey v. Hardy,* 63 Utah 231, 224 Pac. 889, 892 (1924). Thus, the failure to deliver a stock certificate to defendant is immaterial. There is an absence of evidence of any demand for such delivery. In fact, Mr. Robbins' testimony was that — undoubtedly in the pattern of many closely held corporations — "(n)o certificates were issued to anybody" (Tr. 14). The record reflects, therefore, that, although defendant concededly had received no *stock certificate,* he maintained — by reason of his initial agreement — a *stock right.*

Review of pertinent authorities demonstrates that the most significant factor among those undisputed is — far from the nondelivery of the stock certificate — the payment of the agreed consideration, $4,000.00, by the defendant into the corporation at or about the time of

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[2] At all times pertinent to this action, the Utah Business Corporation Act, effective January 1, 1962, was inapplicable. In consequence, citations throughout are to Title 16, Chapter 2 UCA, 1953, then effective.

the initial agreement (Tr. 19-20). *For, by such payment, the contract became nonexecutory, defendant's stock right vested, and he became — at law — a stockholder in Robbins, Inc.* As stated by the Idaho Supreme Court in *Savic v. Kramlich,* 52 Idaho 156, 12 P.2d 260, 262 (1932):

> "When stock is paid for, it is in fact issued, irrespective of the issuance of the certificate which is nothing more nor less than evidence of the stockholder's ownership."

In accord is *Federal Deposit Ins. Corp. v. Gunderson,* 106 F.2d 633 (8 Cir., 1939).

When, therefore, defendant paid in the $4,000.00 he became a stockholder. In this capacity, he had no further obligations toward the corporation. Its obligation was to him as its stockholder.

This Court has recognized the principles here enunciated. It has held that, once the stock agreed upon is paid for, the obligee becomes a stockholder and — upon corporate failure following demand to deliver an appropriate certificate — he may, at his option, either sue the corporation at law for the conversion of the stock or in equity for the delivery of such certificate, *Robey v. Hardy,* supra at 224 Pac. 892; *Coray v. Perry Inv. Co.,* 50 Utah 70, 166 Pac. 672 (1917).

Prior to the second agreement, that of April, 1960, defendant's relationship with Robbins, Inc. had ripened into that of a stockholder. At any time prior to entry into that later agreement, he could have — following demand — compelled issuance of a certificate as evidence thereof. His stock position was clear.

B.

The second agreement of April, 1960, *was one for purchase by Robbins, Inc. of defendant's stockholder interest in the purchasing corporation.*

Given defendant's status as a corporate stockholder prior to the agreement of April, 1960, there is no question that such second agreement constituted a repurchase by the corporation of such stock interest. Defendant testified that the effect of the agreement was to take him "out of the corporation" and to get his "money out" (Tr. 18), and Mr. Robbins' testimony was to the same effect (Tr. 10, 13, 15). A divestiture of defendant's interest in the corporation, i.e. his interest as a stockholder, necessarily required a sale of his stock (Tr. 11).

It is clear, further, that the sale from defendant was to — and the purchase by — Robbins, Inc. Although Mr. Robbins co-signed the note as an individual, it is undisputed that the $1,900.00 with which we are here concerned was paid by the corporation out of its corporate account (Tr. 12-13).[3]

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[3] The fact that defendant's status as a corporate employee terminated at or about the time of the agreement to purchase his stock interest has no bearing on the transaction. There being no evidence that his employment was for a term, the presumption is that it was terminable at will, **Bullock v. Deseret Dodge Truck Center, Inc.,** 11 Utah 2d 1, 354 P.2d 559 (1960); Annos. 11 A.L.R. 740, 100 A.L.R. 835, 161 A.L.R. 709; 35 **Am. Jur., Master and Servant,** §19 at pp. 457-58. It could, thus, have been terminated by either party independent of the purchase of defendant's stock, there being no representation by either defendant or Mr. Robbins that the initial agreement of February or March, 1960 made defendant's status as an employee legally dependent upon his status as a stockholder, or vice-versa.

It should be mentioned in passing that, taken in the light of the objective facts and the applicable law, the elicitation upon cross examination of Mr. Robbins of the conclusion that "actually the original agreement was modified by a later agreement" (Tr. 15)) may mislead. The agreement of April, 1960 patently was not the conclusion of a series of continuing negotiations between the parties initiated in February or March of that year. There were, rather, two separate agreements. Rights under the initial agreement had vested prior to entry into the second agreement, i.e. the one for purchase by Robbins, Inc. of its own stock. The only manner in which the later agreement, *if legal,* modified the former was through changing the status of the parties created and vested under the prior contract.

A case remarkably similar on its facts to the instant controversy, and one which is in accord with the concepts presented both under subdivisions A and B of this Point, is *Mindenberg v. Carmel Film Productions,* 132 Cal. App. 2d 598, 282 P.2d 1024 (1955). The initial agreement, dated March 8, 1948, was that Mindenberg "(p)ending the issuance of stock," "shall have a present 18¾% interest in and to all the assets of said corporation." Thereafter, on April 30, 1948, Mindenberg and the corporation entered into a second, and separate (albeit it modified the status created by the first), contract whereby Mindenberg — in consideration of $26,250.00 payable in installments from the corporation — did "assign, transfer, set over, deliver, acquit and release to Carmel Film Productions, Inc., all of my right, title and interest therein, whether represented by stock or arising out of that certain 'Memorandum of Agreement' between the parties hereto dated March 8, 1948." In the suit, one by Mindenberg to recover unpaid installments, the corporation defended upon the ground that the second agreement was illegal as specifying an unpermissable purchase by it of its own stock. Mindenberg countered by asserting, as does the defendant here, that he had never been issued stock certificates for the 18¾%, and that there was no sale or purchase of corporate stock. The trial court so held, but the Court of Appeals reversed, stating at 282 P.2d 1031 that the lower court's holding:

> "(I)gnores the legal effect of the agreement for 'a present 18¾% interest in and to all of the assets of said corporation . . .' The issuance of the certificate was not essential to plaintiff becoming a shareholder . . . 'Capital stock' means, 'not the shares of which the nominal capital is composed, but the actual capital — i.e. assets — with which the corporation carries on its corporate business' . . . The sale of plaintiff's 18¾% interest was a sale of stock." (Citations eliminated.)

The Court of Appeals then held that Mindenberg had failed to sustain his burden of proving that the payment for the corporation's own stock under the subsequent agreement would be out of surplus, rather than out of capital, as required by California law, and therefore reversed the trial court's judgment for the plaintiff.

In the instant case, as in *Mindenberg*: (1) defendant's percentage holding constituted a holding of stock, even in the absence of the delivery of a stock certificate; and (2) defendant's and Robbins, Inc.'s mutual agreement that defendant return his interest in consideration of the corporation's installment payments constituted a purchase by such corporation of its own stock.

It shall now be demonstrated that here, as in *Mindenberg*, the purchase by Robbins, Inc. from defendant was illegal.

POINT II

THE $1,900 PAID TO DEFENDANT BY ROBBINS, INC. WAS MADE IN THE ILLEGAL AND VOID PURCHASE OF ITS OWN STOCK.

A.

The general rule in Utah is that a purchase by a corporation of its own stock is illegal and void.

The Utah rule on this subject was established by *Pace v. Pace Bros.*, 91 Utah 132, 59 P.2d 1 (1936), *reh. den.*, 91 Utah 149, 63 P.2d 590 (1936). The decision, neither modified nor reversed by subsequent judicial pronouncement, in effect adopted the English common law rule that a corporation may not — absent certain judicially engrafted exceptions or express statutory authority — purchase its own stock, and that any such purported purchase is void, *Trevor v. Whitworth,* 12 App.

Cas. 409 (1887). The holding was premised upon the public policy enunciated by 103-12-4(2) Rev. St., 1933, a penal statute, which rendered it a misdemeanor for any corporate director:

> "To divide, withdraw or in any manner, except as provided by law, pay to the stockholders, or any of them, any part of the capital of the corporation."

On petition for rehearing, this Court further extended the holding to prohibit such purchases out of "surplus," i.e. restricted permissible payments to stockholders to dividends, unless otherwise provided by the aforementioned judicial exceptions or statutory authority, *id.,* 63 P.2d 591.

In consequence, at the behest of intervening judgment creditors of the corporation,[4] the former stockholder was prohibited from enforcing notes and mortgages given him in exchange for corporate stock.

This Court in *Pace* placed heavy reliance upon the damage done to creditors — prior, present or future — through the dissipation of capital inherent in a purchase by a corporation of its own stock, stating at 59 P.2d 5:

> "It may be remarked that it would give little comfort to a creditor if he found all the assets gone but the treasury full of the corporation's own stock certificates paid for by its assets."

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[4] Whose credits and resulting judgments were subsequent to the notes and mortgages given plaintiff, **Abstract of Record** (State Library), pp. 7, 14, 32, 33.

This reasoning closely mirrored that of Lord Herschell in his opinion in *Trevor v. Whitworth,* supra (decided upon seriatim opinions), when he said that creditors:

> ". . . have a right to rely, and were intended by the Legislature to have a right to rely, on the capital remaining undiminished by any expenditures outside these limits, or by the return of any part of it to the shareholders."

For comprehensive authority additional to that cited in *Pace* to the effect that treasury stock cannot be considered a true asset of a corporation and that, by the very nature of the corporate structure, it cannot own any part of itself so that such a transaction is in reality a reduction of equity, see footnote 5, *Fultz v. Anzac Oil Corp.,* 240 F.2d 21, 22-23 (5 Cir., 1957).

The statute upon which this Court in *Pace* predicated the public policy against such a reduction of equity was equally effectual at all times here pertinent. 78-13-4(2) UCA, 1953 is identical to 103-12-4(2) Rev. St. 1933, except for certain provisions relative to preferred stock not here applicable (Tr. 12). Additionally, 18-2-17 Rev. St., 1933 — which this Court in *Pace* indicated would contribute weight to the public policy pronounced had it been in effect at the time of the transaction there considered, 59 P.2d 3 — was incorporated in 16-2-15 UCA, 1953.

Therefore, unless otherwise "provided by law," the payments made by Robbins, Inc., to defendant pursuant to the stock purchase were illegal and void.

B.

The subject stock purchase was not authorized by 16-2-16 *UCA*, 1953.

By L. 1951, ch. 23, §2, the legislature specified certain conditions under which a corporation permissively "may purchase or redeem one or more shares of any and all of its own capital stock," 16-2-16 UCA, 1953. This constituted a "provision of law" which, when applicable, would justify a departure from the general rule enunciated in *Pace, Shumaker v. Uetx Exploration Co.,* 157 F. Supp. 68, 74 (D. Utah, 1957).

Two factors which reflect upon the scope and purpose of the enactment require examination at the outset. First, as shall become apparent, 16-2-16 constituted both a codification of judicial exceptions recognized by *Pace* and a legislative creation of additional exceptions. Second, the Utah legislature did not follow the precedent of its California counterpart. Prior to 1929, based upon a similar penal statute, the rule adopted by *Pace* had applied in California and—in fact—this Court in *Pace* relied heavily upon California precedents, 59 P.2d 3, 6-7. In that year, however, the California legislature enacted a statute which gave positive authorization to corporations, subject to certain specified exceptions, to purchase their own stock; for the legislative history, see *Goodman v. Global Industries,* 80 Cal. App. 2d 583, 182 P.2d 300 (1947). In Utah, to the contrary, there remained after 1951 a positive prohibition against such purchases, subject only to the permissive exceptions specified.

From the first factor, it is concluded that judicial precedent will prove—in some instances — helpful in interpretation of 16-2-16. From the second factor, it is concluded that Utah law derogates against corporate self-purchase unless it can be demonstrated that a given permissive condition exists.

The latter conclusion is supported by the decision of this Court in *White v. Western Empire Life Ins. Co.*, 11 Utah 2d 227, 357 P.2d 483, 484 (1960), in which the requirement of "substantial evidence" was specified to justify the finding of an exception. The *White* decision is cited by 6A *Fletcher Cyc. Corps.* §2848 at p. 372 (1963 cum. supp. at p. 12) in support of the following statement:

> "However, even if the right to purchase its own stock is recognized, the right to purchase should be confined within strict limits . . ."

With this background, particular examination of the 16-2-16 exceptions in the context of the undisputed facts will be undertaken. The only two statutory segments which have conceivable applicability are subdivisions (a) and (f). The Trial Court relied upon both, finding: (1) "(I)f this was a stock transaction it would appear to the Court that it is clearly exempt by Section 16-2-16, Utah Code, 1953, Subsection (a)"; and (2) "(I)t clearly appears from the evidence that the financial structure of Robbins Travel Corporation was not in any way affected by the transaction" (R. 16).

Analysis will demonstrate that neither finding is supported by any evidence, let alone substantial evidence, and that — in fact — the undisputed facts and applicable law impel the conclusion that neither permissive condition exists in this case.

1.

16-2-16(*a*) *is inapplicable to this case.*

16-2-16(a) permits corporate purchase of its own stock "(t)o collect or compromise, in good faith, a debt, claim or controversy with any shareholder."

Although the Trial Court was less explicit than might be desired in expressing its reasons for finding condition (a) fulfilled, it would appear that the key is "controversy." This conclusion is reached by the process of elimination. It is patent that there was, prior to the agreement of April, 1960 (which agreement was one, at law, by Robbins, Inc., to purchase its own stock), no "debt" or "claim" flowing from defendant to the corporation or vice-versa. Thus only the "controversy" category remains.

The only evidence bearing upon any "controversy" was that, following defendant's entry—as an owner and officer—into the affair of Robbins, Inc., Mr. Robbins grew dissatisfied with his efforts. They then decided mutually that defendant would get "out" of the corporation. The April agreement ensued (Tr. 13, 15, 18).

Consideration of condition (a) demonstrates that this type of "controversy" is not of the sort which fulfills the statutory requirement for a departure from the general rule prohibiting purchase by a corporation of its own stock.

In the first place, *the "controversy" testified to was not between Robbins, Inc., as an entity and the defendant, but rather between Mr. Robbins and the defendant.* To allow a dominant individual in a corporation to "compromise" his differences with a fellow stockholder through the *corporate* purchase of the other's stock—and the consequent dissipation of the capital fund held for past, present and future creditors—would not only expand condition (a) beyond its apparent dictate that the "debt, claim or controversy" involve the corporation, but would run counter to the well-established policy of the law that capital stock shall not be purchased by the corporation to benefit any individual stockholder in an intra-corporate fuss. *The remedy of the individual shareholder is, rather than "raiding" the corporate creditor's fund, to purchase for his own account and at his own expense the stock of the fellow shareholder with whom he has a "controversy".* Both Lord Herschell and Lord Macnaghten in *Trevor v. Whitworth,* supra, dealt with the legality of a purchase by the corporation to remove dissenting stockholders.

According to the former:

> "I can quite understand that the directors of a company may sometimes desire that the stockholders should not be numerous, and that they should be persons likely to leave them with a free hand to carry on their operations. But I think it would be dangerous to countenance the view that, for reasons such as these, they could legitimately expend the moneys of the company to any extent they please in the purchase of its shares. No doubt if certain shareholders are disposed to hamper the proceedings of the company, and are willing to sell their shares, they may be bought out; but this must be done by persons, existing shareholders or others, who can be induced to purchase the shares, and not out of the funds of the company."

Said the latter:

> "Who are the shareholders whose continuance in a company the company or its executives consider undesirable? Why, shareholders who quarrel with the policy of the board, and wish to turn the directors out; shareholders who ask questions which it may not be convenient to answer; shareholders who want information which the directors think it prudent to withhold. Can it be contended that when the policy of directors is assailed they may spend the capital of the company in keeping themselves in power, or in purchasing the retirement of inquisitive and troublesome critics?"

It is interesting to note, in this regard, that the Supreme Court of Delaware has recently held officers of a corporation liable for accounting to shareholders when they cause such corporation, for their own benefit, to purchase its own stock, even though corporate capital was not thereby impaired, *Bennett v. Propp,* 187 A.2d 405 (Del., 1962).

Summarizing the first deficiency in the Trial Court's application of condition (a): (1) no "controversy" of any type between defendant and the corporation was shown, which would justify Robbins, Inc.'s purchase of its own stock; and (2) there is an established legal interdiction against "raids" on corporate capital to resolve intra-corporate business disputes—it is up to one disputant to buy out the other.

Secondly, and equally determinative, a consideration of accepted legal definition and a reading of condition (a) in its entirety leads to the conclusion that, as used in the context, the word "controversy" does not refer to any dispute—business, social or otherwise, but rather to justiciable disputes, ones which are subject to adjudication. This is so for three reasons.

(1) In its legal sense, the word "controversy" refers to justiciable controversies. Hence *Black's Law Dictionary* (4th Ed), at p. 400 defines the word thusly:

> "Controversy — A litigated question; adversary proceeding in a court of law; a civil action or suit, either at law or in equity; a justiciable dispute."

As a legal term, the word "controversy", therefore, embodies the concept of a dispute which has ripened into justiciability.

(2) The conclusion reached by a consideration of

the legal definition of the word "controversy" is further strengthened by an examination of the entire condition (a). In context, the word appears disjunctively, as follows: "debt, claim or controversy." Both "debt" and "claim" are easily identifiable as terms referring to justiciable disputes. Under the rule of interpretation, *noscitur a sociis,* the meaning of a word is known from the words which accompany it. Had the legislature intended the word "controversy" to be applied to any dispute, whether justiciable or not, it would not have utilized the terms "debt" and "claim", for they would have been superfluous. It is inherent in the drafting of the disjunctive that the legislature desired to allow collection or compromise of *any* justiciable dispute.

(3) The conclusion that a justiciable dispute was contemplated is strengthened by an examination of established law at the time of the enactment of 16-2-16. Both under the English rule and under the *Pace* decision, it was recognized that a corporation might receive its own stock to collect or compromise an outstanding obligation, *Pace v. Pace Bros.,* supra at 59 P.2d 3; Levy, "Purchase by an English Company of its own Shares", 79 *U. of Pa. L. Rev.* 45, 55-56 (1930). In this light, it appears likely that condition (a), at least, was a codification of common law, to be judged by common law standards. If so, it clearly applies only to justiciable disputes and excludes the settlement of non-justiciable disputes, particularly when they are between two shareholders and not between a shareholder and the corporation, see Levy, "Purchase by a Corpo-

ration of its own Stock", 15 *Minn. L. Rev.* 1, 15, 31-32 (1930).

Whatever controversy the record reveals as a precedent to the April agreement (by which the corporation arranged to purchase its own stock) was between Mr. Robbins and defendant, not between Robbins, Inc., and defendant. It was, moreover, non-justiciabel. A business disagreement between shareholders, absent some grounds for suit, is not a province of the courts.

The Trial Court erred in finding condition (a) to be met.

2.

16-2-16(*f*) *is inapplicable to this case.*

Condition (f) allows corporate self-purchase "(i)n any case where the use of the funds or property of a corporation for such purchase or redemption would not cause the impairment of that portion of its assets acquired as consideration for its shares . . . ." Its prime effect is to restrict the meaning given "capital" by *Pace* at 63 P.2d 591. Following its enactment, purchase by a corporation of its own stock could be made out of surplus. The statutory definition of "capital" is in accord with the general contemporary concept, 18 *C.J.S., Corporations,* §193(b) at p. 616.

The evidence regarding the financial condition at the times of payment of moneys received by defendant is undisputed. Robbins, Inc. was insolvent at all such times. (Tr. 12). It had no surplus. The purchase was thus bound to impair[5] the capital of the corporation, i.e. "that portion of its assets acquired as consideration for its shares." The financial structure of the corporation was obviously adversely affected, for $1,900.00 in cash assets was paid to purchase treasury stock which as previously noted, could not properly be classed as an asset, *Fultz v. Anzac,* supra.

In *Cleveland v. Jencks Mfg. Co.,* 54 R.I. 218, 171 Atl. 917, 918 (1934), the Rhode Island Supreme Court, in considering a statute which—as ours—prohibits corporate self-purchase resulting in impairment of capital, stated:

> "It is obvious that an insolvent corporation would not possess assets sufficent to purchase shares of its own stock without impairing assets."

That is the precise situation which is here encountered. At the time of payments, the corporation was insolvent.

And the time of payment controls. Wormser, "Corporation's Power to Acquire its Stock", 24 *Yale L.J.* 177, 186-87 (1915) discusses the situation where "the contract of purchase is made when the corporation is solvent, but the corporation becomes insolvent before payment is made on completed." Citing *In the matter of Fechheimer Fischel Co., Bankrupt,* 212 Fed. 357 (2d Cir., 1914), *cert. den.* 234 U.S. 760 (1914) the article concludes that the financial condition at the time

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5 "To make worse; to diminish in quantity, value, excellence, or strength; to deteriorate; damage; as, to **impair** health," **Webster's New International Dictionary** (2d Ed), p. 1246.

of payment, not at the time of contract, is the significant fact. In accord is the more recent case of *In re Matthews Const. Co.*, 120 F. Supp. 818, 821 (S.D. Calif., 1954).

The Trial Court's conclusion that "the financial structure of Robbins Travel Corporation was not in any way affected" was clearly erroneous. The condition created by 16-2-16(f) was not met.

POINT III

THE FACT THAT ROBBINS, INC.'S DEBT TO PLAINTIFF AROSE SUBSEQUENT TO ITS ILLEGAL PAYMENTS TO DEFENDANT IS IMMATERIAL.

The Trial Court found that "the transaction between the Robbins Travel Corporation and the defendant Luman took place long prior to the indebtedness of the Robbins Travel Corporation to the plaintiff" (R. 17). The record is clear that both the stock purchase agreement of April, 1960, and the payments thereon took place at least a year prior to contraction of the indebtedness upon which plaintiff took judgment. (Tr. 14).

But of what importance is this? *Pace v. Pace Bros.*, supra, settled Utah law that a subsequent creditor may attack a previous unlawful sale of stock. The holding makes sense, for the illegal damage to the corporate structure is as harmful to future as to present creditors. According to this Court at 59 P.2d 7:

"Future as well as present creditors should be able to rely on the implied representation that the corporation holds assets as represented by its outstanding stock."

The *Pace* decision has not been modified or overruled in this regard, either by this Court or by the legislature. The attempt to impugn plaintiff's status by its being a future creditor is therefore nugatory.

If payment for a corporation's own stock is illegal, it can recover from the payee, even though the contract of purchase is fully executed, for—although the parties are in pari delicto—the capital of the company has been pro-tanto reduced by the payments and public policy requires the intervention of the courts, 6*A Fletcher Cyc. Corps.* §2852 at pp. 388-89; see *Murphy Wholesale Grocery Co. v. Skaggs,* 67 Utah 487, 248 Pac. 127, 130 (1926). Plaintiff, pursuant to URCP 64D, garnisheed this liquidated indebtedness from defendant to Robbins, Inc., its judgment debtor. In view of the law and the facts, the Trial Court erred in refusing judgment as prayed.

CONCLUSION

In February or March, 1960, defendant became a stockholder in Robbins, Inc. In April, 1960, Robbins, Inc. purchased such stock, delivering a note to defendant. The corporation, while insolvent, made payments in the amount of $1,900.00 pursuant to that note. The transaction of April, 1960, and payments made pursuant thereto were illegal and void as against public policy. Plaintiff, as a judgment creditor of Robbins, Inc., has standing—through garnishment—to raise such illegality, and should have been granted judgment by the Trial Court as prayed. It is prayed on appeal that this Court reverse the Trial Court's decree of dismissal and remand with the direction to enter judgment against defendant and in favor of plaintiff in the sum of the judgment debt owing by Robbins, Inc. to plaintiff, but not to exceed $1,900.00.

Respectfully submitted,

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